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In the Supreme Court of the United States

OCTOBER TERM, 1945

No. 682

H. SMITH RICHARDSON, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum opinion of the Tax Court (R. 43–65) is not officially reported. The opinion of the Circuit Court of Appeals (R. 196–204) is reported in 151 F. 2d 102.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on August 17, 1945. (R. 205.) A petition for rehearing filed September 1, 1945 (R. 206), was denied on September 25, 1945 (R. 212). The petition for a writ of certiorari was filed on

December 19, 1945. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether the Tax Court correctly determined for federal gift tax purposes, the value of closely held stock of Piedmont Financial Company, Inc., on December 20, 1935, the date the taxpayer made gifts thereof to his children by way of transfers in trust.

2. Whether the accumulation in 1935 for the benefit of taxpayer's children of income in trusts created in 1932 by taxpayer's wife wherein the taxpayer was made trustee with the power to revoke the trusts and vest title to the principal in himself constituted gifts of such income by taxpayer to his children within the meaning of Section 501 of the Revenue Act of 1932.

3. Whether the accumulation of the income for the benefit of the taxpayer's children in the 1932 trusts was not subject to a gift tax on the theory that such accumulation was by virtue of a "release of a power to appoint" within the meaning of Section 452 (c) of the Revenue Act of 1942, as amended.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra*, pp. 15–22.

STATEMENT

The facts with regard to the question of the fair market value, for gift tax purposes, of certain stock of Piedmont Financial Company, Inc., were in part stipulated and in addition certain expert testimony was introduced both by the taxpayer and the Government. The facts with regard to the question whether the taxpayer is subject to a gift tax as a result of the accumulation of the income in the trusts created by taxpayer's wife in 1932 were entirely stipulated. (R. 18–32.) As found by the Tax Court (R. 43–57), the facts relating to each of the questions presented may be summarized as follows:

1. On December 20, 1935, the taxpayer made five gifts in trust, one for the benefit of each of his children, of certain shares of capital stock of Vick Chemical, Inc.,[1] and of a total of 5,100 shares of capital stock of Piedmont Financial Company, Inc. (R. 43–44.)

In his gift tax return the taxpayer valued the Piedmont stock at $99.11 per share. The Commissioner determined that this stock had a fair market value on December 20, 1935, of $95.509 a share. Before the Tax Court, the taxpayer contended that the Piedmont stock had a fair market

[1] The question raised in the court below as to the valuation of the stock in Vick Chemical, Inc., is not presented in the taxpayer's petition for a writ of certiorari. (See Petition, p. 3, footnote 1.)

value on December 20, 1935, of not in excess of $50 per share. (R. 44.)

Piedmont Financial Company, Inc., was organized in 1925 and on December 20, 1935, had outstanding 100,000 shares of common stock of no par value, which had never been listed and was held by 33 stockholders, all of whom were members of the Richardson family, consisting of the taxpayer and his brother and the wife and family of each. The business of the corporation was chiefly that of investing its funds in stocks and securities of other companies. (R. 49.) Its portfolio of investments on December 31, 1935, consisted of securities having a cost or book value, which was not materially different on December 20, 1935, of $6,392,543.43. (R. 50–51.)

A tabulation of the mean prices at which securities owned by Piedmont sold on the stock exchange on December 20, 1935, is set forth in the findings. (R. 51–53.) As reflecting the market value of the securities owned by Piedmont, its stock was worth $98.08 per share on that date. (R. 24, 61.)

The net earnings of Piedmont ranged from $133,268.56 to $604,317.75 in the years 1927 to 1936, inclusive, except that in the year 1931 there was a loss of $296,333.57. In the year 1935, the total net earnings of the company were $323,-973.65. The net earnings per share in these years ranged from $1.33 to $6.04 per share, except that

in the year 1931 there was a loss of $2.96 per share. In the year 1935, the earnings per share were $3.24. In the same years, the dividends paid per share were as follows: None in 1927; $4.95 in 1928; $1.575 in 1929; none in 1930, 1931 and 1932; $2.85 in 1933; $4.35176 in 1934; $2.52 in 1935, and $0.7875 in 1936. (R. 53.)

The balance sheets of Piedmont as of June 30, 1934, 1935 and 1936 are included in the findings. (R. 53–54.)

An index to the testimony of the expert witnesses may be found at R. 88.

The Tax Court found that the fair market value, on December 20, 1935, of the 5,100 shares of Piedmont Financial Company, Inc., was not less than $95.509 per share (R. 54), and the Circuit Court of Appeals affirmed (R. 202).

2. On or about May 15, 1932, the taxpayer's wife made five transfers in trust to the taxpayer as trustee of an aggregate of 42,500 shares of Piedmont stock. The trust instruments were identical, except for the names of the several beneficiaries, who were the five children of the taxpayer and his wife. (R. 54.)

Each trust provided that the trustee should collect the trust income, and, until the beneficiary became twenty-one years of age, apply to the beneficiary's maintenance, education or benefit so much thereof as he, in his discretion, should deem advisable, the remainder to be accumulated and

reinvested for the child's benefit; after the beneficiary became twenty-one years old, the trustee should pay to him or her such portion of the annual trust income, or any part of the accumulation which he, in his discretion, might determine; and when the beneficiary became 35 years old, the trustee was to pay over all of the accumulations and income therefrom, to the beneficiary. Upon the death of the beneficiary, the trust should terminate and the principal and undistributed income should be delivered as the beneficary directed by last will and testament. (R. 54–55.) The trustee was given complete powers of management. (R. 55.)

Each agreement provided that, during his lifetime, the taxpayer "may cancel and terminate this agreement" and, in the event of his doing so, the corpus of the trust fund should absolutely vest in him free from all trusts. (R. 55.)

In 1935, $106,675 of income was accumulated and $900 was paid to the beneficiaries. (R. 56.)

On December 30, 1941, the taxpayer terminated the trusts and received in his individual right the 42,500 shares of Piedmont stock which had constituted the corpora of the trusts. (R. 56.)

The Tax Court found (R. 56) that the accumulation of the income for the benefit of the children named as beneficiaries in the trust instruments constituted taxable gifts from the taxpayer to such beneficiaries, and the Circuit Court of Appeals affirmed (R. 204).

ARGUMENT

1. The decision below with respect to the value of the Piedmont Financial Company, Inc., stock is correct and does not conflict with the decision of any other Circuit Court of Appeals, nor is it contrary to the Treasury Regulations.

The taxpayer's assertion (Pet. 6–8) of conflict between the decision below and the decision of the Circuit Court of Appeals for the Third Circuit in *Laird* v. *Commissioner,* 85 F. (2d) 598, and the Treasury Regulations, rests upon the assumption that the Tax Court, in determining the value of the Piedmont stock, gave no consideration to any other factor than the value of the assets owned by the Piedmont company. Contrary to the taxpayer's assumption, it is entirely clear from the Tax Court's opinion that it did not refuse or fail to give consideration to any other factor than the value of the Piedmont assets. The Tax Court said (R. 61):

> After having considered all of the relevant financial statistics and the facts disclosed by the record, including the opinions of the expert witnesses who testified herein, and having given due weight to those factors relevant and pertinent to the determination of the fair market value of this stock, we conclude that the stock of the Piedmont Financial Co. which was the subject of the gifts in question had, on December 20, 1935, a fair market value of not less than $95.509 per share.

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Among the facts disclosed by the record, and included within the Tax Court's findings, were the company's net worth, a history of its earnings, a history of its payment of dividends, and the company's balance sheets for three years, embracing the critical date. In the *Laird* case, *supra*, the Circuit Court of Appeals reversed the decision of the Board of Tax Appeals (now the Tax Court) because the Board did not give any consideration whatever to the earning and dividend-paying capacity of the stock there in question. In the present case, it is clear that the Tax Court did give consideration to such factors.

It is, of course, the duty of the Tax Court to weigh the evidence, and its decision will not be disturbed upon review if it is supported by substantial evidence and is in accordance with the proper standards of law. *Dobson* v. *Commissioner*, 320 U. S. 489, rehearing denied, 321 U. S. 231. The taxpayer does not attack the sufficiency of the evidence to support the Tax Court's finding of value, complaining only that the Tax Court failed to apply a proper standard of value. The majority of the court below were of the opinion that the Tax Court had used a proper standard (R. 202), and the decisions of that court in *Weber* v. *Rasquin*, 101 F. (2d) 62, and *Commissioner* v. *McCann*, 146 F. (2d) 385, which the taxpayer relies upon in the present case, demonstrate that that court recognizes as the proper standard

of value a rule which is in accord with the Treasury Regulations and with the decision of the Circuit Court of Appeals for the Third Circuit in the *Laird* case, *supra*. Neither the opinion of the court below in the present case, nor the opinion of the Tax Court, is contrary to those earlier decisions of the Second Circuit.

2. The decision of the court below affirming the holding of the Tax Court that the accumulation of income in the trusts created in 1932 by taxpayer's wife constituted gifts from the taxpayer to his children subject to gift tax is correct and there is no conflict among the Circuit Courts of Appeals.

The taxpayer here had the undisputed right to cancel and terminate the trust agreements and thereupon to receive the corpora of the trust funds absolutely and free from all trusts. (R. 55.) On December 30, 1941, subsequent to the year here involved, he in fact exercised this power and received in his own name and individual right the shares of stock which had constituted the corpora of the trusts. (R. 56.) Under the trust agreements the accumulations of income are to be paid over to the respective beneficiaries when he or she shall become thirty-five years of age. (R. 26, 55.) These accumulations of income could not be withdrawn by the taxpayer after they were set aside for his children (R. 21, 56), and so there is no question as to the com-

pleteness of the gifts if otherwise within the statute.

The position of the Commissioner, sustained below, is that the trust property was, for tax purposes, the property of the taxpayer. (R. 65.) In the case of *Richardson* v. *Commissioner,* 42 B. T. A. 830, affirmed, 121 F. (2d) 1 (C. C. A. 2d), certiorari denied, 314 U. S. 684, rehearing denied, 314 U. S. 714, it had already been held that the income of these trusts was taxable against the taxpayer as his income.[2] The basis of that decision was that the taxpayer's unfettered control over the corpora of these trusts was the equivalent of the ownership of the property for tax purposes. *Helvering* v. *Clifford,* 309 U. S. 331; *Helvering* v. *Horst,* 311 U. S. 112.

Section 501 (a) of the Revenue Act of 1932 (Appendix, *infra*) imposes a tax upon the transfer of property by gift, and Section 501 (b) (Appendix, *infra*) provides that the tax shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible. This language of the statute is broad enough to include property and property rights of every description, and the effort of Congress was to reach every kind and type of transfer by

[2] It was stipulated (R. 21) that the trusts in question in the present case created by the taxpayer's wife in 1932 are the same trusts as those involved in that case.

gift. *Smith* v. *Shaughnessy,* 318 U. S. 176; *Robinette* v. *Helvering,* 318 U. S. 184.

The control over the disposition of the income here involved which the taxpayer enjoyed by virtue of his control over or substantial ownership of the source of that income requires the conclusion that the transfer of that income constituted a gift from the taxpayer subject to a gift tax.

The case of *Commissioner* v. *Solomon,* 124 F. (2d) 86 (C. C. A. 3d), which the taxpayer asserts (Pet. 9–10) is in conflict with the present case, is distinguishable. In that case the court points out (pp. 89–90) that the taxpayer did not have as full dominion over the property as if she owned it because she could not have claimed the corpus of the trust for herself. It was this absence of ownership or control over the source of the income which the court relied upon as the distinguishing fact. In the present case, as has been pointed out, the taxpayer did control and, for tax purposes, was the owner of the source of the income here in question.

The acquiescence by the Commissioner in *Clark* v. *Commissioner,* 47 B. T. A. 865, referred to by the taxpayer (Pet. 10) as establishing a settled administrative policy, may not be regarded as an acceptance of the construction which the Board of Tax Appeals in that case placed upon the applicable gift tax provisions of the 1932 Act, but

only as an acceptance of the fact that the retroactive provisions of Section 452 (c) of the Revenue Act of 1942 (Appendix, *infra*) made the transfer nontaxable in any event. In that case the taxpayer had expressly amended the deed of trust by striking out the provision which had given her the unqualified power to amend the trust. The Commissioner had ruled that this amendment of the trust whereby the taxpayer relinquished the power over the trust corpus was in effect a transfer of that corpus to the successor beneficiaries named in the trust. While the decision of the Board of Tax Appeals in that case that the relinquishment of the right to amend the trust was not a gift within the gift tax provisions of the 1932 Act was deemed erroneous, it was thought that the transaction fell within the provisions of Section 452 (c) of the Revenue Act of 1942, made applicable to all calendar years prior to 1943, which were to the effect that a release of a power to appoint before January 1, 1943 (subsequently extended to July 1, 1946), shall not be deemed a transfer of property by the individual possessing such power.

The case of *Royce* v. *Commissioner,* 46 B. T. A. 1090, relied upon by the taxpayer (Pet. 10), involved a question of the federal estate tax and is not applicable here.

3. The present case does not, as argued by the taxpayer (Pet. 12–16), fall within the provisions

of Section 452 (c) of the Revenue Act of 1942. That section, as amended, as pointed out above, provides that a release of a power to appoint before July 1, 1946, shall not be deemed a transfer of property by the individual possessing such power.

Here the taxpayer had the power to cancel and terminate the trust agreements and upon such termination and cancellation to receive the corpora of the trust funds absolutely and free from all trusts. (R. 55.) The taxpayer never released this power, but in fact, in December, 1941, subsequent to the year here involved, exercised that power in his own favor and received in his own name and individual right the stock which had constituted the corpora of the trusts. (R. 56.)

There was also no release of a power of appointment over the interim income within the meaning of Section 452 (c) of the Revenue Act of 1942. This income is to be considered the income *of the taxpayer* because of his control over the disposition of the income which derives from his control of the source. That power was never released. That a time arrives when the taxpayer no longer has control over the income does not signify a release of a power to appoint within the meaning of Section 452 (c) any more than does the loss of control over any property which has been the subject of a gift. It merely attests the completeness of the gift.

The fact that Section 452 (c) of the Revenue Act of 1942 has no express provision relating to interim income similar to the provision in Section 1000 (e) of the Internal Revenue Code, added by Section 502 (a) of the Revenue Act of 1943, c. 63, 58 Stat. 21, relating to the estate tax, does not indicate that Congress intended to exempt from the operation of the gift tax statute interim income which is the subject of a taxpayer's disposition by virtue of a taxpayer's continued control over the source of that income. Cf. *Burnet* v. *Guggenheim*, 288 U. S. 280.

CONCLUSION

The decision below is correct; there is no conflict of decisions; and the case does not call for further review.

Respectfully submitted.

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JANUARY 1946.